THE DEBT DEAL

Implications for Massachusetts

Updated January 2012

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Executive Summary

ON AUGUST 2, 2011 Congress passed the Budget Control Act of 2011, commonly known as the "debt deal." The law raised the nation's debt ceiling, averting what would have been an unprecedented and catastrophic abandonment of the country's commitment to pay its bills. In exchange for increasing the U.S. borrowing authority, the debt deal requires at least $2.1 trillion in deficit reduction over the next ten years.

Almost half of the impending cuts will come from discretionary programs other than defense, such as state grants for housing assistance, funding to help families heat their homes during New England's harsh winters, food and drug safety, and biomedical research. About one-third of this discretionary spending typically goes to local municipalities, but this is likely going to change as programs are scaled back to meet the spending caps imposed by the debt deal.

For most programs, the debt deal does not mandate which programs receive cuts or by how much. Instead, the law sets overall spending caps on two broad categories – defense and domestic spending. Congress must then decide during the regular annual appropriations process, how to live within those caps.

These cuts could hardly be coming at a worse time. Already, programs that support middle-class or low-income families in Massachusetts are experiencing shrinking resources. In times of financial crisis and high unemployment, the need for vital safety-net services grows just as a diminished tax base leaves programs with less funding. Massachusetts lawmakers and residents must actively fight to protect the funding and programs that form the building blocks of our 21st century economy: a high education and healthy workforce, high-quality healthcare, clean technology and biomedical industries, and research institutions that draw bright workers and billions of dollars into the state.

The Debt Deal in Three Steps

Step 1 of the Budget Control Act: $917 billion in federal spending cuts (See Appendix A)

- The debt deal established caps on the amount of money that can be spent through the annual budget process, reducing federal spending on discretionary programs by $917 billion. The caps are not placed on specific programs; instead they are placed on two broad categories:
    - Security Spending: Department of Defense (DOD), Homeland Security, Veterans' Affairs, National Nuclear Security Administration, and foreign affairs.
    - Non-security: Domestic spending.

- Which programs actually get cut – and by how much – will be determined by the regular Congressional appropriations process.
- Programs at risk for cuts, based on what Republicans have targeted in previous budget proposals, include:
    - National Institutes of Health (NIH), which brings $2.5 billion in medical research funding to Massachusetts and supports 35,000 jobs across the state
    - The Low Income Home Energy Assistance Program (LIHEAP), which provided over $235 million in heating and cooling assistance for more than 200,000 Massachusetts households in 2011
    - Clean energy projects, which have brought $450 million in federal funding to the state over the past two years. There are upwards of 30,000 clean technology jobs in Massachusetts.
- Entitlement programs, including Medicare, MassHealth, and Social Security are exempt from these cuts.

STEP 2 OF THE BUDGET CONTROL ACT: THE "SUPER COMMITTEE," TASKED WITH REDUCING THE DEFICIT BY AT LEAST $1.2 TRILLION (SEE APPENDIX B)

- The debt deal established a 12-member, bipartisan Congressional committee, which was tasked with developing a plan to reduce the deficit by at least $1.2 trillion.
- The Super Committee could have proposed spending cuts, tax increases, or any combination of the two.
- On November 21, 2011 the Super Committee reported that it was unable to reach an agreement, triggering Step 3 of the law.

STEP 3 OF THE BUDGET CONTROL ACT: AUTOMATIC SPENDING CUTS OF $1.2 TRILLION WILL BEGIN TO TAKE EFFECT STARTING JANUARY 2013

- Automatic cuts will be split 50%-50% between:
    - Defense programs (DOD and the National Nuclear Security Administration); and
    - Non-defense programs (i.e., NIH, LIHEAP, Centers for Disease Control, Food and Drug Administration).
- While lawmakers will be able to decide how to distribute the automatic cuts required to discretionary spending beginning in FY 2014, the rest of the cuts (i.e., all cuts in 2013 and cuts to mandatory spending made beginning in FY 2014) will be done evenly across-the-board.
- Programs that serve the low-income population are largely exempt, including: Medicaid, Social Security, food stamps, Earned Income Tax Credit, Child Tax Credit, Temporary Assistance for Need Families military pay, veterans' benefits, and Medicare benefits (though doctors and hospitals face a cut of up to two percent in reimbursement from the Medicare program).

INTRODUCTION

Over the past several decades, Massachusetts has devoted enormous resources to laying the foundation for a strong and resilient economy. Massachusetts has developed a world-class education system, with more than 100 colleges and universities and 350,000 college students in the Greater Boston Area. With this well-educated workforce, we are transforming a blue collar past into a green collar future. Cutting-edge industries of the 21st century – clean technology, biotechnology, and healthcare – have taken root and flourished in the Commonwealth. A strong foundation is a major reason that Massachusetts has weathered the battering impact of the recession better than many other states. At 6.8 percent, Massachusetts' unemployment rate is 1.7 percent lower than the national average. And our median income beats the national average by nearly $20,000.

The debt deal is poised to undermine this progress by threatening programs that are needed more than ever in light of the lingering economic crisis. The United States has constructed a safety-net system to catch those who slip from financial security during times of hardship, helping them regain their economic footing until the storm passes. But the past four years have illustrated the unfair paradox of this system. As the economy stumbled in 2008, banks stopped lending and the availability of credit from markets shrank. Companies, unable to access credit and therefore grow, enacted hiring freezes or began laying off workers. Without a paycheck or the health insurance that employment often provides, workers and their families must lean more heavily on safety-net services – MassHealth for health insurance, housing and food assistance, help with heating their home, and financial aid to attend school. Shrinking paychecks results in fewer resources flowing into state and local coffers to fund the services that are needed today more than ever.

Instead of bolstering programs that help people get back on their feet and find a job, the debt deal calls for trillions of dollars in cuts that support these systems. Instead of helping state and local governments plug the budget holes that were blown open by the recession and make up for the end of $1.5 billion in federal stimulus funding, the debt deal will force cutbacks to grants that allow states to meet the basic needs of their residents.

Where these cuts fall will largely be determined by the decisions of Congressional appropriators over the next decade. Congress has already started implementing the cuts to discretionary spending that were required for FY 2012. Whatever decisions are made will have a major impact on Massachusetts' education system, its healthcare programs, and the economy at large. While the debt deal prevented our nation from default, the deep spending cuts required by the law could jeopardize what is already a sputtering and jobless economic recovery.

The following is an explanation of the process, timeline and scope of the debt deal in the aftermath of the termination of the Super Committee and an analysis of the deal's impacts on Massachusetts.

STEP 1 - $917 BILLION IN SPENDING CUTS

BACKGROUND

In exchange for raising the debt ceiling and avoiding default, the debt deal required that federal spending be slashed by $917 billion over the next ten years, starting with a $21 billion reduction in FY 2012 and a $42 billion reduction in FY 2013. The spending cuts will primarily come from three categories: security spending, non-security spending, and debt service.

The law does not place caps on specific programs; such decisions will be made by Congressional appropriators during the regular budget process. However, the law does outline broad caps on both security and non-security spending. Security spending – which includes the Department of Defense (DOD), Department of Veterans Affairs (VA), Department of Homeland Security (DHS), National Nuclear Security Administration (NNSA), and foreign affairs – will be reduced by $350 billion. Non-security discretionary spending, or domestic spending that requires annual appropriations, will be reduced by $393 billion. The remainder of the savings comes primarily from debt service - money saved by reducing the principal on our debt. These cuts, which will occur over a period of ten years and began in the FY 2012 appropriations process, are back-loaded to avoid making major spending reductions now while the economic recovery is still precarious.

These cuts do not impact mandatory programs, or programs that do not require annual appropriations. Exempted mandatory spending includes Medicare, Medicaid and CHIP (MassHealth in Massachusetts), Social Security, food stamps, and Temporary Assistance for Needy Families. Anything else could be on the chopping block.

In November 2011, Congress passed its Transportation-Housing-Urban Development, Agriculture, and Commerce-Justice-Science spending bills. The remaining nine spending bills, including Labor, Health, and Human Services, were passed in late December and were consistent with the spending caps imposed by the debt deal. While the Republican budget blueprint laid out earlier in the year had called for massive reductions to everything from education to Medicare and Medicaid, strong opposition from Democrats and some Republicans succeeded in providing most programs level funding (or smaller cuts) from FY 2011. Unless the debt deal is repealed or modified, this will change as the debt deal requires deeper and deeper cuts in the coming years.

Massachusetts Impact: Domestic Spending at Risk

National Institutes of Health

The National Institutes of Health (NIH) is an engine of economic growth and job creation. As the world's preeminent medical research institution, NIH is our best hope for finding cures, improving treatments, and gaining a better understanding of the complex causes of diseases that affect millions of Americans. NIH also has a key role to play in our economic recovery, with its 27 institutes supporting more than 350,000 scientists and research personnel nationwide, as well as the acquisition of goods and services from every state. Though Massachusetts ranks 15th in population, it ranks 2nd in the race for federal NIH research dollars. During FY 2010, NIH funding brought $2.5 billion dollars to the Commonwealth and supported 35,000 jobs.

Congressman Markey has led the fight in the House of Representatives to protect NIH funding, though it has been an uphill battle. In FY 2011, NIH sustained budget cuts of $317 million in FY 2011, jeopardizing countless research projects that already are underway in Massachusetts. In the spring of 2011, Congressman Markey was joined by 117 of his Democratic colleagues in calling for full funding for NIH so that it can sustain its mission of improving health through medical science breakthroughs and maintaining international leadership in biomedical research. These efforts led to Congressional appropriators providing NIH an increase of nearly $300 million in FY 2012.

Clean Energy

The clean technology sector employs upwards of 30,000 people in Massachusetts.[1] Employment in the industry has increased by 65 percent in the past three years, becoming the 10th largest sector in Massachusetts. The U.S. Department of Energy has been a major partner in Massachusetts' rise to global leadership in this sector. During the last two years, more than $450 million in federal funding has supported more than 120 clean energy projects in the state. New programs like the Advanced Research Project Agency—Energy (ARPA-E), which is modeled after the highly successful defense-oriented Defense Advanced Research Projects Agency program, have awarded multi-million dollar research grants to leading Massachusetts companies like FloDesign Wind Turbine, Agrivida, 1366 Technologies, and others. Federal research awards, manufacturing grants, and loan guarantees have helped MIT and A123 Systems in Watertown develop world-leading vehicle battery technologies that may ultimately break America's addiction to oil. Support from the Department of Energy enabled the establishment of the Wind Technology Testing Center in Charlestown, the foundation of which is anticipated to become a thriving offshore wind hub.

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[1] *Sizing the Clean Economy: A National and Regional Green Jobs Assessment*. Brookings Institute. 13 July 2011.

[2] *Community Services Block Grant, State Plan and Application*. Department of Housing and Community Development. August 2010.

The FY 2012 energy spending bill that passed out of the House of Representatives in July 2011 was disastrous for clean energy interests in Massachusetts. Republicans insisted on a nearly 40 percent cut to renewable energy and energy efficiency programs, which amounted to nearly $2 billion below the President's budget request. At the same time, Republicans increased investments in mature technologies like nuclear and fossil energy in the bill.

Fortunately, despite the lowered spending levels required by Step 1 of the Debt Deal, the Senate rejected the House's extreme proposal. What became law through the 2012 energy spending bill is similar to 2011 spending levels and largely protects Massachusetts' interests in clean energy. Funding for renewable energy and energy efficiency is set at $1.8 billion, far short of the President's request of $3.2 billion but $500 million more than the Republican's House-passed position. Funding for the Energy Department's Science program is similar to 2011 levels as well, at $4.9 billion. The ARPA-E program, received $275 million for 2011, an increase over the $180 million it received in 2011. This prestigious program, which is modeled after the highly successful defense-oriented DARPA program, has been a boon to Massachusetts with multi-million dollar research awards going to leading companies and institutions like FloDesign Wind Turbine, Agrivida, 1366 Technologies, A123 Systems, MIT, and the University of Massachusetts at Amherst among others.

House Republicans continued their assault on renewable energy through the Department of Energy's Loan Guarantee Program. Last April, in bringing the government to the brink of closure, Republicans successfully passed into law a rescission of $18.2 billion in loan guarantees for clean energy and efficiency. Not surprisingly, they left in $22.5 billion for the nuclear industry and $8 billion for coal. Unfortunately, this pattern continued in the FY 2012 spending bill, as no funds were provided for loan guarantees for clean energy. This could prove devastating for projects like Cape Wind, a proposed offshore wind energy facility of the coast of Massachusetts, which are very close to moving forward but need the boost that low-cost government financing can help provide.

Clean energy will almost certainly remain a target for Republicans in future budget cycles, as they relentlessly pursue the repeal of laws and regulations protecting everything from clean water and air to energy efficient light bulbs. Their budget blueprint from April 2011 proposed slashing alternative energy investments by 70 percent in 2012 and 90 percent over the next three years. Then in August, even as Republicans held America's credit hostage and demanded aggressive deficit slashing, they protected the $4 billion in annual tax breaks available to oil and gas companies. Clean energy programs and environmental protections have driven Massachusetts' blossoming clean energy economy, and a vigorous defense will need to be mounted to protect them in the face of Republican opposition.

COMMUNITY SERVICES BLOCK GRANTS

The Community Services Block Grant (CSBG) program has sustained significant cuts in past years. CSBG funds Community Action Programs, which are the federal government's only comprehensive approach to addressing the needs of vulnerable citizens and helping struggling Americans get the services they need to achieve economic security. Last year, these programs provided critical support such as employment services, education, and housing to 20.7 million Americans facing an array of enormous challenges ranging from extreme poverty and disability to lack of employment and shelter. They created or saved 18,432 jobs nationwide.

During FY 2010, in Massachusetts alone, the CSBG program funded 24 community action programs that were able to reach over 600,000 individuals across the state, with a focus on economic self sufficiency, affordable housing for the homeless, and targeted funding for low-income youth.[2]

Action for Boston Community Development (ABCD), a widely respected community services program funded by CSBG, is a great example of this program. ABCD makes a difference for 80,000 individuals and their families in the Commonwealth every day. ABCD supports a network of hundreds of neighborhood offices, Head Start centers, family planning sites, and fuel assistance sites throughout the state, which help residents get back on their feet, find jobs and pay taxes. Moreover, every CSBG dollar is multiplied 20 times over in private and public funds raised to support community programs and meet needs. ABCD is helping more than 26 thousand low-income families survive harsh winters with its fuel assistance program, providing Head Start and child care services for 2,400 children and their families, and beginning recruitment of 5,000 inner city youth for the agency's summer jobs and education program. ABCD has also launched the Earned Income Tax Credit campaign that will help close to 10,000 working poor families access up to $6,500 each in tax credits.

Congressman Markey led the effort, joined by 84 of his colleagues, to protect CSBG funding and was successful in securing $680 million for FY 2012. Massachusetts is expected to receive approximately the same amount from FY 2011, or about $17 million.

LOW-INCOME HOME ENERGY ASSISTANCE PROGRAM

The Low-Income Home Energy Assistance Program (LIHEAP), which sustained a $400 million reduction in FY 2011, again found itself on the chopping block in this budget cycle. LIHEAP assists families to heat their homes during the frigid New England winters and cool them during the summer. In Massachusetts alone,

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[2] *Community Services Block Grant, State Plan and Application*. Department of Housing and Community Development. August 2010. http://www.mass.gov/Ehed/docs/dhcd/cd/csbg/fy2011-2012csbgdraftplan-app.pdf.

LIHEAP helped more than 200,000 families heat their homes last winter.[3] This assistance is especially vital in light of skyrocketing energy costs. Over the last five years, the average cost of heating a home with heating oil jumped nearly $1,000, from $1,337 to $2,291.

Unfortunately, the FY 2012 spending bill cuts LIHEAP by 24 percent, resulting in just $132 million for Massachusetts (down from $175 million the year before). Such a heavy cut could leave thousands in the cold or result in reduced benefits for all.

Small Business Innovation Research Program

Agencies use a small percentage of their research and development (R&D) budgets to fund the Small Business Innovation Research program (SBIR), a source of federal research and development grants for small businesses. To date, over $28 billion has been awarded by the SBIR program to various small businesses nationwide. However, cuts to R&D programs will necessitate reductions to the SBIR contributions made by the eleven participating agencies: DOD, the Departments of Health and Human Services, Agriculture, Commerce, Education, Energy, Homeland Security, and Transportation; the Environmental Protection Agency, National Aeronautics and Space Administration, and National Science Foundation.

In the last four years, Massachusetts' innovative companies have received 2,215 SBIR awards, totaling almost $759 million. After California, Massachusetts receives the second highest number of awards annually and receives the most awards per capita in the nation.[4] In the 27-year history of the SBIR program, Bay State companies have received 17,361 awards, bringing $4 billion into the state to promote innovative research with commercial applications.[5] Firms like Watertown-based Radiation Monitoring Devices (RMD) are working on the cutting edge of innovation. RMD recently received a $220,000 SBIR award to develop a device for measuring capillary blood flow and detecting the onset of shock, helping to advance our understanding of heart and vascular diseases.

Foreign Affairs

Over the next 10 years, $350 billion (of the total $917 billion) will need to be cut from our nation's security spending. The inclusion of foreign affairs in the definition of security spending, which includes anti-HIV/AIDS efforts, family planning programs, USAID, the Peace Corps, and any program within the State Department, makes it likely that these programs will sustain heavy cuts in order to avoid reductions to programs the military

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[3] *LIHEAP Household Report - Federal Fiscal Year 2011*. Executive Office of Housing and Economic Development for Massachusetts. 24 July 2011. http://www.mass.gov/Ehed/docs/dhcd/cd/liheap/003fy2011householdrpt.pdf.

[4] "Small Business Innovation Research Awards." *SBIR.gov*. 08 Sept. 2011. http://www.sbir.gov/past-awards.

[5] "Small Business Innovation Research Awards." *SBIR.gov*. 08 Sept. 2011. http://www.sbir.gov/past-awards.

deems a higher priority, such as hardware. The FY 2012 State and Foreign Operations spending bill cut $6 billion from last year's level.

Medical Research

In addition to foreign affairs, medical research spending in these security departments is a likely target for budget reductions in the coming years. The FY 2011 DOD budget included $1.175 billion for research and development within the Defense Health Program. Of that amount, approximately $400 million was directed to Congressionally Directed Medical Research Programs (CDMRPs), which fund research for a wide range of diseases and conditions including Alzheimer's, autism, and spinal cord injuries. Massachusetts' researchers received $35 million in CDMRP grants in FY 2010. Of this, $23.7 million in grants were awarded to teaching hospitals, including a group of researchers at Dana-Farber Cancer Institute who are using their $464,000 grant to improve our understanding of how breast cancer metastasizes in the body.

CDMRPs were cut by about $20 million in the FY 2012 defense spending bill. While some new programs were added, breast cancer funding was cut by $30 million and ALS funding was cut by nearly $2 million.

STEP 2 – The Super Committee

In addition to the initial round of $917 billion in spending cuts, a bipartisan joint committee was tasked with laying out a plan to reduce the deficit by at least $1.2 trillion over ten years. The Super Committee could have proposed spending cuts, tax increases, or any combination of the two. This "Super Committee" of 12 members of Congress – six from the Senate and six from the House of Representatives – had until November 23, 2011 to pass their proposal by a simple majority. Congress would have voted on the proposal by December 23. However, on November 21, 2011 the Super Committee Members, which included six Republicans and six Democrats, announced that they were unable to produce a bipartisan agreement in advance of their statutory deadline of November 23, 2011.

While numerous proposals were discussed by both parties, none were successful in gaining bipartisan agreement. Republicans demanded steep cuts to entitlement programs like Medicare, Medicaid, and Social Security, but they refused to include in the agreement any new revenues through tax increases on millionaires and billionaires. Democrats insisted that any proposal include a balanced mix of spending cuts and substantive tax increases on the wealthiest Americans. In the end, the Democrats and Republicans on the Super Committee were unable to reach agreement, and their efforts ended in gridlock.

What Happens After the "Super Committee"?

Background

Without a bipartisan agreement from the Super Committee, a process to make $1.2 trillion in additional spending cuts to everything from Medicare to medical research to defense is now set in motion. These cuts begin to take effect beginning January 2, 2013 unless Congress and the President agree to legislation repealing or modifying the automatic cuts. Unlike in Step 1, this round of $1.2 billion in cuts cannot be back-loaded in later years in order to avoid jeopardizing an already shaky economic recovery.

In Step 3 of the process, an additional $110 billion in spending will be cut each year (over the next nine years). Half of the cuts ($55 billion per year) will come from defense programs, which in this step includes only the DOD. The other half will come from domestic spending, with some cut from mandatory programs and the bulk cut from discretionary programs. The mandatory cuts will be applied automatically and across the board to every program that is not explicitly exempted. However, key programs are protected from the automatic cuts, including Medicare benefits, MassHealth, and programs on which low-income families rely. Mandatory programs not protected include certain farm subsidies and Vocational Rehabilitation State Grants.

One other mandatory spending program – Medicare payments to providers and insurance companies – are partially protected. The payments are reduced, but the cut is capped at two percent. The Congressional Budget Office (CBO) estimates that in FY 2013, Medicare providers would experience a cut of $11 billion. Because Medicare costs are projected to rise, the total amount of the cut will add up to approximately $123 billion over nine years and could make it harder for seniors to get the care they need if Medicare providers exit the market due to reimbursement rates they determine to be too low. According to a recent study by the American Hospital Association, an automatic two percent cut would also cost 194,000 jobs nationwide.[6]

The discretionary cuts are generally handled differently. The law caps the amount of discretionary spending Congress is allowed, but it remains up to lawmakers to determine how best to live within those caps.[7] Discretionary programs potentially on the chopping block include vital programs like medical research funding for NIH, food safety funding for FDA, and low-income heating assistance through LIHEAP.

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[6] *The Negative Economic Impact of Cuts to Hospital Funding: Potential Jobs Loss*. Tripp Umbach, Sept. 2011.
[7] Discretionary cuts for 2013 are handled differently, as explained in the following section.

The breakdown of the automatic cuts is as follows:

Spending Reductions from FY 2013-FY 2021
(in billions)

	Required Cut Per Year	Required Cut Over Nine Years
Defense[8]	$55	$495
Domestic	$55	$495
Subtotal	*$110*	*$990*
Savings from Lowered Interest Payments	$24	$216
Total	***$134***	***$1,206***

The law includes a formula to determine, among the domestic spending cuts, how much must be cut from mandatory programs and how much from discretionary spending.[9] Of the $55 billion cut from domestic spending per year, approximately $16 billion will come from mandatory domestic programs (e.g. farm subsidies and limited cuts to Medicare providers) and about $39 billion from discretionary domestic programs (e.g. any program that relies on annual appropriations). The new discretionary caps are illustrated in the following chart.

Revised Statutory Limits on Discretionary Spending Under Automatic Cuts
(in billions)

	Caps on Spending After Step 1 ($917 in Spending Cuts)			Caps on Spending After Step 1 and Step 3 ($917 + $1,200 in additional cuts)		
Fiscal Year	Total Discretionary	Defense	Domestic	Total Discretionary	Defense	Domestic
2013	$1,047	$546	$501	$953	$491	$462
2014	$1,066	$556	$510	$973	$501	$472
2015	$1,086	$566	$520	$994	$511	$483
2016	$1,107	$577	$530	$1,016	$522	$494
2017	$1,131	$590	$541	$1,035	$535	$505
2018	$1,156	$603	$553	$1,065	$548	$517
2019	$1,182	$616	$566	$1,093	$561	$532
2020	$1,208	$630	$578	$1,120	$575	$545
2021	$1,234	$644	$590	$1,146	$589	$557

[8] In Step 1 of the debt deal, the cuts were divided between "non-security spending" and "security spending," which included the DOD as well as foreign affairs, the VA, and other programs. However, this round of cuts requires a reduction to "defense," which now includes just the DOD. Foreign affairs, the VA, and the other departments are now excluded from the definition of "defense" spending, and thus are not able to shoulder the burden with the DOD.

[9] The defense budget is essentially all discretionary spending so this is largely irrelevant to defense spending.

Protected Programs

Not everything is on the chopping block under automatic cuts. Key programs that serve low-income individuals and families are exempt from these cuts, including:

- Medicaid and CHIP (MassHealth)
- Medicare benefits
- Social Security
- Military pay
- Veterans benefits
- Earned Income Tax Credit
- Child Care Tax Credit
- Temporary Assistance for Need Families
- Food stamps

Applying the Automatic Cuts in 2013

The first automatic cuts required under Step 3 of the debt deal do not take effect until January 2, 2013. This was done intentionally. In crafting the debt deal, lawmakers included a buffer of slightly more than a year from the time the Super Committee would announce the results of its negotiations to the time automatic cuts would begin in the event of a deadlock.

The sequestration of discretionary spending is handled differently for FY 2013 than it is for the remainder of the years covered by the debt deal, FY 2014-2021. With regard to FY 2013, automatic, across-the-board cuts will be made to whatever funding is provided for that year. Because the cuts take effect one-quarter of the way into the fiscal year, spending authority for federal agencies will have already been determined and at least partially doled out. The Office of Management and Budget will thus be responsible for rescinding funding from the various agencies ("sequestration") in order to meet the level of cuts required by the debt deal.

As for mandatory spending, the sequestration is required for each year for FY 2013-FY 2021. Unless the debt deal were modified or repealed, Congress will not have the ability to determine where these cuts fall. In other words, required cuts to mandatory spending will be carried out evenly and automatically in each year.

The following chart[10] from the Center for Budget and Policy Priorities provides a breakdown of the required cuts for 2013 in light of the Super Committee's inability to produce a plan:

Sequestration in 2013 if Appropriations Match 2013 Caps
In billions of dollars

	Resources Before Sequestration	Sequestration	
		Dollar reduction	Percent reduction
Defense	**$726**	**$54.7**	
Military personnel funding, assumed to be **exempt** (est.)	136	0	0.0%
Other non-war funding for 2013	410	38.0	9.3%
Subtotal, amount subject to caps	546		
War funding, outside of caps (estimated)	90	8.3	9.3%
Unobligated balances from prior years (estimated)	90	8.3	9.3%
Non-defense discretionary (NDD) programs	**501**	**38.6**	
Non-exempt programs	423	38.5	9.1%
Veterans' health and Pell grants, **exempt** (estimated)	72	0.0	0.0%
Health centers and Indian health, **2% limit** (estimated)	6	0.1	2.0%
Non-exempt mandatory programs	**605**	**16.1**	
Medicare payments to providers and plans, **2% limit**	542	10.8	2.0%
Other non-exempt mandatory programs	63	5.2	8.2%

Note: The percentage cut in non-exempt, non-defense discretionary funding of 9.1 percent is deeper than the percentage cut in non-exempt mandatory funding of 8.2 percent. The two percentages would be identical if the basic non-defense sequestration had been allocated proportionally across all non-exempt programs, and if the additional cuts needed to offset the effect of the 2 percent limit on the sequestration of some health programs had also been allocated proportionally across all other non-exempt programs. But the Budget Control Act (BCA) does not work that way. To begin with, the 2 percent limit on the cut to discretionary health centers and Indian health is offset only by increasing the cut to other non-defense discretionary (NDD) programs. Similarly, the exemption of Pell grants and VA medical care from sequestration must be offset by deeper cuts in other NDD programs. Thus, non-exempt mandatory programs do not help offset the exemption for Pell grants and VA medical care or the 2 percent limit on the cut to discretionary health centers and Indian health. In contrast, the BCA specifies that the 2 percent Medicare limit is offset by deeper cuts to both non-exempt mandatory programs and non-exempt NDD programs. This structure results in somewhat different sequestration percentages applying to those two categories of non-exempt non-defense programs.

In other words, in 2013 defense programs would receive a uniform 9.3 percent reduction and domestic programs would receive a uniform 9.1 percent reduction. For example, each research institute within the NIH would receive the same reduction of approximately 9.1 percent. Similarly, the food safety, drug safety, and radiological devices and products safety accounts within the FDA would also receive the same reduction. Tax credits included in the health care reform law to help middle and low-income families afford their health insurance deductibles, co-pays, and other cost-sharing expenses will also be reduced because they are not refundable (and, thus, not considered exempt under the law). Only Medicare provider payments and Community Health Centers have a separate cut specified of two percent.

10 Kogan, Richard. *How the Potential 2013 Across-The-Board Cuts in the Debt Deal Would Occur*. Center for Budget and Policy Priorities, 2011

Applying the Automatic Cuts Beginning 2014

The automatic cuts are applied differently in FY 2014 – FY 2021, when Congress will determine which discretionary programs get cut from FY 2014-2021 through the regular appropriations process. The spending cuts among the discretionary programs are achieved by limiting the maximum amount that Congressional appropriators can provide. It will be up to Congress to operate within those new caps and pass spending bills that fall within these new limits and can garner the signature of the President. If the appropriations bills were to exceed the statutory limitations, then automatic, across-the-board cuts would be implemented to bring the spending bill below the cap.

Again, such decisions do not apply to mandatory spending, which is not subject to the annual appropriations process. From FY 2014-FY 2021, mandatory programs (i.e. Medicare provider payments, farm price supports) will face automatic, across-the-board reductions. Again, Medicare provider payment cuts will remain capped at two percent. The following chart[11] from CBPP provides a yearly breakdown of the cuts required from defense, non-defense discretionary (NDD), and mandatory programs:

What Will Happen in 2014 through 2021
In billions of dollars

	2014	2015	2016	2017	2018	2019	2020	2021
Defense caps before reduction	556	566	577	590	603	616	630	644
Required reduction, dollars	-54.7	-54.7	54.7	-54.7	54.7	-54.7	54.7	-54.7
Required reduction, percent	9.8%	9.7%	9.5%	9.3%	9.1%	8.9%	8.7%	8.5%
Resulting level of caps	501	511	522	535	548	561	575	589
NDD caps before reduction	510	520	530	541	553	566	578	590
Required reduction, dollars	-38	-37	-36	-36	-35	-34	-33	-33
Required reduction, percent	7.4%	7.1%	6.8%	6.6%	6.4%	6.1%	5.8%	5.5%
Resulting level of caps	472	483	494	505	518	532	545	557
2% Medicare sequestration, dollars	-11.4	-12.0	-12.9	-13.4	-14.1	-15.1	-16.1	-17.2
Non-exempt mandatory cuts other than Medicare, dollars	-5.3	-5.7	-5.7	-5.4	-5.3	-5.2	-5.1	-5.0
Non-exempt mandatory cuts other than Medicare, percent	7.4%	7.1%	6.8%	6.6%	6.4%	6.1%	5.8%	5.5%

[11] Kogan, Richard. *How the Across-The-Board Cuts in the Budget Control Act Will Work* Center for Budget and Policy Priorities, 2011

MASSACHUSETTS IMPACT

SENIORS' ACCESS TO HEALTHCARE PROVIDERS

The debt deal reduces payments to Medicare doctors, hospitals and insurance companies by two percent, which could further exacerbate doctor shortages in Massachusetts and cause access problems for seniors requiring medical care. Massachusetts continues to experience a shortage of a wide range of health care providers, particularly those in family and internal medicine. Data from the 2010 Practicing Physician Survey indicate that retention rates among physicians in Massachusetts is worsening, with 35 percent of practicing physicians reporting that their ability to retain doctors has become more difficult over the past several years. At the same time, vacancy rates remain high throughout the state, with 63 percent of practicing physicians reporting difficulty in filling vacancies.

While the two percent reduction each year raises significant access concerns, the greater worry is the need for the "doc fix." Provider groups had been hoping that the Super Committee would include in their plan a "doc fix" - an overhaul of the Sustainable Growth Rate (SGR), the formula that calculates Medicare's payments to doctors and hospitals. The formula was originally supposed to rein in Medicare spending by reducing payments to providers if Medicare costs grew too quickly. For most of its existence, the formula has called for cuts, though Congress routinely overrides them. Doctors had hoped that the flawed SGR – which currently calls for a 27 percent reduction in 2013 – would be replaced in the Super Committee's proposal to avoid this perennial problem. As of January 2012, Congress is still negotiating a way to avoid a payment cliff for Medicare providers once the current SGR patch expires next month. Cuts of the magnitude required by the current formula, were they to go into effect, could force many physicians to close their practices, lay off staff, or limit the number of Medicare and TRICARE patients they can see.

NATIONAL INSTITUTES OF HEALTH

At a Senate hearing in May 2011, NIH Director Dr. Francis Collins testified to the role that the agency plays in driving the biomedical research industry. "NIH support for biomedical research institutions," Dr. Collins said, catalyzes business activity…Such institutions constitute reservoirs of skilled, knowledgeable individuals and thereby, attract companies that wish to locate their operations within such 'knowledge hubs.'"[12] Nowhere is this a truer statement than in Massachusetts. The state's researchers bring in about $2.5 billion in NIH grants each year, keeping the state at the cutting edge of innovative biomedical research and supporting 35,000 jobs. Though Massachusetts ranks 15th in population, it ranks 2nd in the race for federal NIH research dollars.

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[12] *Department of HHS, National Institutes of Health, Fiscal Year 2012 Budget Testimony*, 112th Congress Cong. (2011) (testimony of Francis Collins, M.D., Ph.D.)

NIH enjoyed bipartisan support in the past, but it remains a challenge just to ensure that NIH's funding keeps pace with inflation and that research projects already underway can continue. In fact in FY 2011, the NIH budget sustained a cut of more than $300 million.

In FY 2013, NIH is scheduled to face a cut of 9.1 percent as required by the debt deal. Assuming the FY 2013 NIH budget is close to its current level, this would equal a $3 billion reduction for biomedical research and would represent, by far, the largest cut in the program's history. It would also come on top of the $317 million in budget cuts that the agency already sustained in FY 2011. If lawmakers do not take action to protect NIH, it could face additional cuts in FY 2014 and beyond.

Ongoing research projects in Massachusetts and throughout the country would be jeopardized as the size and number of research grants available shrank. For example, at Tufts University in Medford, scientists are working on regenerating bone to fix massive defects caused by injury, illness, or congenital malformations. A company in Malden is currently investigating the role of prenatal alcohol in Sudden Infant Death Syndrome (SIDS) to improve our understanding of a disease that claims the lives of 2,500 newborns every year. These and other research projects could be shelved if NIH is cut further.

Teaching hospitals could also be severely impacted by NIH funding reductions. Of the $2.5 billion in NIH grants that go to Massachusetts awardees each year, approximately half goes to teaching hospitals, which educate and train the next generation of medical professionals, conduct cutting-edge research, and provide care for the nation's most vulnerable and sickest populations. Teaching hospitals in the Boston area include Tufts Medical Center, Cambridge Health Alliance, Massachusetts General Hospital, Boston Medical Center, Beth Israel Deaconess Medical Center, Children's Hospital Boston, Brigham and Women's Hospital, Faulkner Hospital, Lahey Clinic, Massachusetts Eye and Ear Infirmary, Carney Hospital, St. Elizabeth's Medical Center, Dana-Farber Cancer Institute, and VA Boston Healthcare System. Every person in America is one phone call or doctor's visit away from needing the important research these institutions conduct, whether that's improving our ability to diagnose colon cancer at Tufts Medical Center or better managing heart failure at the Brigham.

Low- Income Heating Assistance Program

A 9.1 percent cut to LIHEAP, the program that helps low-income families heat and cool their homes, would mean a FY 2013 cut of approximately $300 million (based on the FY 2012 budget). Massachusetts share of the cut, based on the amount of LIHEAP funding the state has receive in past, could be expected to equal approximately $12 million. With the average LIHEAP benefit equal to about $300, such a drastic reduction could mean 40,000 household go without aid.

COMMUNITY SERVICES BLOCK GRANTS

In FY 2013, the CSBG program will be reduced to approximately $620 million from $680 million in FY 2013. Massachusetts could lose about $1.5 million of its regular CSBG allocation and possibly more in the following years.

PUBLIC HEALTH

The Centers for Disease Control and Prevention provides about $140 million for Massachusetts' public health efforts each year, with the bulk of funding subsidizing vaccines for uninsured and underinsured children, detecting and responding to emergencies such as tornadoes and hurricanes, and dealing with food-borne illnesses and infectious disease outbreaks. Much of the funding supports the Massachusetts Public Health Department, which is especially vital in light of the state's budget constraints. Last year, the Public Health Department received approximately $47 million to prepare for emergencies and natural disasters, combat childhood obesity, and improve the state's immunization infrastructure. Sanofi Pasteur received grant funding to develop and produce their smallpox vaccine, and ABT Associates received $5 million to evaluate the safety and effectiveness of the H1N1 influenza vaccine among pregnant women.[13]

In FY 2013, the stream of public health funding (like all non-defense discretionary programs) can expect to face a 9.1 percent cut, which could mean about $13 million less for Massachusetts. Programs at the CDC are especially vulnerable because of the substantial cuts they sustained in earlier rounds of budget cuts. In FY 2011, federal funding for the CDC declined by $740 million.

HIV/AIDS

About 20,000 individuals living with HIV/AIDS in Massachusetts can receive help for the lifesaving and costly medications they need through the Ryan White HIV/AIDS Program, which serves as a last resort for low-income and uninsured patients. Last year, the Massachusetts Department of Public Health as well as Community Health Centers around the state received more than $20 million through the Ryan White program to provide services for these patients, whose annual cost of care can run to about $100,000.[14] Cuts to the Ryan White Program, or to CDC funding that helps states provide free or subsidized HIV testing, could be a death sentence for these patients.

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[13] USAspending.gov
[14] USASpending.gov

GRADUATE MEDICAL EDUCATION

At this time, it is unclear how the federal Office of Management and Budget (the agency ultimately responsible for carrying out this stage of the debt deal) will treat Indirect Graduate Medical Education (IME). If they decide it is not exempt from the automatic cuts, Massachusetts teaching hospitals could face heavy losses. Medicare provides IME payments to reimburse teaching hospitals for the added costs of training residents and treating severely ill, expensive patients. IME is thus a payment to Medicare providers, but it is not payment for services (which are subject to the two percent reduction).

Reducing IME payments would cost Massachusetts hospitals – and the state economy – millions of dollars. The Boston Teaching Hospitals alone employ 77,800 people. Reducing IME payments could force hospitals to lay off workers including medical residents (physicians in training), their supervising physicians, nurses, clinical researchers, and other hospital staff. This would greatly contribute to the current medical workforce shortage, which is projected to reach 35,000 surgeons and 27,000 medical specialists nationwide by 2020.

These estimates do not take into account the indirect impact on employment. Teaching hospitals are often the largest employers in their communities and major economic engines. Thus, additional job losses are likely across other business sectors, such as retail, service, and manufacturing that benefit from the direct expenditures of teaching hospitals and their employees. Businesses that are recipients of spending by hospital patients, patients' visitors, medical students and their visitors will also be negatively impacted by IME cuts.

These possible cuts to IME come on top of decisions made by states, including Massachusetts, to eliminate or drastically reduce Medicaid funding for medical education. Additionally, significant Medicare payment reforms to hospitals contained in the Affordable Care Act - which called for a total reduction of $155 billion - are just now being implemented.

Teaching hospitals play a critical role in training tomorrow's doctors, providing specialized services such as trauma centers, pediatric ICUs and transplant centers, and conducting groundbreaking medical research that save lives. Cuts to this programs could have a devastating impact on the ability of teaching hospitals to fulfill these critical missions.

As a major driver of the economy, teaching hospitals are a unique resource and a significant factor in life sciences companies locating and growing in Massachusetts and in many other parts of the country. The U.S. has the world's best physicians and nurses because we have the world's best teaching hospitals. Significant cuts to

Medicare IME payments could jeopardize the U.S.'s international status as a leader in the life sciences arena as our economy emerges from the worst recession in generations.

DEFENSE

Defense programs will face heavy reductions since half of the cuts in this phase of the debt deal must come from the defense sector. Because of the Super Committee's inability to produce a plan, $55 billion in spending cuts are now required from defense appropriations. This constitutes a 9.3 percent reduction from current levels.

These cuts could pose a threat to Massachusetts companies, which received $15.6 billion in defense contracts in FY 2009, or 85 percent of all federal contract dollars awarded to the state. The defense industry also supported more than 115,000 jobs that year. The defense industry has been growing in economic importance to Massachusetts since 2001, when total defense related economic activity in Massachusetts totaled $10.6 billion. It has since more than doubled to $26 billion and supports nearly 50,000 additional jobs.[15]

In FY 2009, four businesses received 65 percent of all federal defense contracts to Massachusetts. These entities then subcontracted work to thousands of smaller businesses, serving as engines of innovative technologies throughout the Bay State. Contracts awarded to these companies and organizations - Raytheon ($4.58 billion), General Dynamics ($2.13 contracts), MIT ($1.75 billion) and General Electric ($1.68 billion) - employ Massachusetts residents and keep the state at the forefront of technological innovation.

Massachusetts companies are conducting precision manufacturing, engineering, and R&D that is vital to military operations, and Massachusetts possess human intellectual capital, which has been the key draw in bringing companies to the area. While these factors would favor Massachusetts companies, massive cuts to defense programs on top of the $350 billion cut under Step 1 of the debt deal could still have a major impact on this industry.

MEDICAL RESEARCH WITHIN THE DEPARTMENT OF DEFENSE

Medical research spending within the DOD would also be subject to automatic cuts. The FY 2011 budget included $1.175 billion for research and development within the Defense Health Program. Of that amount, $675 million was designated for Congressionally Directed Medical Research Programs (CDMRPs), which fund research for a wide range of diseases and conditions, including Alzheimer's, autism, and spinal cord injuries. Massachusetts researchers depend heavily on these grants. They received $35 million in CDMRP grants – or

[15] *The Defense Industry in Massachusetts: Current Profile and Economic Significance*. Issue brief. Economic and Public Policy Research Unit, University of Massachusetts Donahue Institute, Dec. 2010.

more than five percent of the total amount awarded – in FY 2010.[16] Of this, $23.7 million in grants were awarded to teaching hospitals, including a group of researchers at Dana-Farber Cancer Institute who are using their $464,000 grant to improve our understanding of how breast cancer metastasizes in the body.

CONCLUSION

The economic downturn has forced layoffs and battered state budgets across the country. While Massachusetts is no exception, the state has weathered the recession better than most thanks in large part to the strength of its technology, defense, higher education, and health sectors. As a hub for the world's premier academic and research facilities, Massachusetts attracts and retains a highly educated workforce and cutting-edge companies. Because of the competitiveness of these institutions, Massachusetts also receives a disproportionately large share of federal grants and contracts to support everything from its health care programs to medical research to the development of defense technologies.

While this source of funding has been beneficial to the Massachusetts, it also means the state is especially vulnerable to drastic reductions in federal spending. Currently, a third of the state budget comes from federal funds that now face the possibility of significant cuts over the ten years of the debt deal. This is exactly the wrong time for cuts to programs on which middle-class and low-income Massachusetts families rely. Though tax revenues in Massachusetts are projected to grow by half a billion to a billion dollars, the state faces a budget shortfall of nearly $2 billion. And unlike last year, Massachusetts will no longer have the $1.5 billion in stimulus funding to help plug the hole. What America's economy needs is support for our vulnerable residents and our struggle cities and town *today*, with deficit reduction efforts occurring once employment picks up and the economy is no longer teetering on the brink of another recession.

The cuts required by the debt deal and the spending cuts that Republicans are currently seeking to offset the extension of the payroll tax cut will fall on those who – after battling through the financial downturn for the last several years – are least able to bear them. Americans living on the edge of poverty. Families once secure in the middle-class pushed to the brink by a pink slip or unexpected illness. Seniors living on fixed incomes. City and state governments trying to plug widening holes in their budgets.

Congressional Republicans are already calling for a repeal of the cuts to defense programs. But we cannot accept a rollback of the cuts to America's bloated nuclear weapons programs while allowing draconian cuts to

[16] "Small Business Innovation Research Awards." *SBIR.gov*. 08 Sept. 2011. http://www.sbir.gov/past-awards.

programs that support the middle-class to take effect.

Perhaps the greatest underlying concern is that the debt deal's spending cuts will undermine job growth. Cut NIH funding and researchers are out of work. Reduce SBIR grants and small businesses shut their doors. Block transportation funding, and construction companies crumble along with our roads and bridges. With more people out of work, the state's tax revenue base shrinks. The budget gap widens. More programs and services are slashed. And the vicious cycle continues.

The best way to reduce our debt and deficit and jump-start our economy is to put people back to work. The challenge, in deciding which cuts to make, is to ensure this priority remains at the forefront.